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MEMORANDUM

Friday, September 27, 1996

TO: Alan Levin
Ron Jacobi
Jim Free

TO:
Linda Carpenter
(4 pages)

TO: Bill Hargrave

FROM: Jack Valenti *Jack Valenti*

The MPAA member companies have a problem. How do we find some way to protect, partially or totally, our creative works once the digital VCRs hit the marketplace?

The answer is: We have an opportunity to put in place a design that will give us some limited control over unauthorized copying. It's my judgment that if we don't grab this brass ring it may never come round again.

Six months ago we cut a deal (after tormenting negotiations) with CEMA, the Consumer Electronic Manufacturing Association. This deal mandated through congressional legislation copy control circuitry in all digital recording devices. Alas, we discovered that while we could mandate 'dumb' VCRs, we could not insert the

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same electronics in 'smart' computers, which have the capability of recording movies.

So - we are now working with CEMA and the computer industry seeking a structure based primarily on voluntary encryption and copy control standards backed up anti-circumvention legislation. (I know, this sound complicated, and it is.) We have to take this voluntary course because the computer industry steadfastly refuses to agree to any legislative mandates.

Difficult technical issues are raining down on us. But DECISIONS have to made, and soon. I need your blessing to move the process forward, striking a deal with CEMA and the computer industry to implement a voluntary encryption-based copy control system.

Your representatives in these long, exhausting negotiations are Ron Jacobi, Linda Carpenter, and Jim Free.

I suggest you may want to consult with your representatives to fill you in on some of the entrails of this most complicated negotiation. A status summary is attached.

But, we must move. We cannot stay inert. Either we go forward, or we leave the arena. Please let me know which direction you want MPAA to go.

FOR OUTSIDE COUNSEL'S
EYES ONLY

DIGITAL VIDEO LEGISLATION A Status Summary

OBJECTIVES

To control the unauthorized copying of prerecorded movies (e.g. digital video discs) and movie transmission services (e.g. satellite and cable pay-per-view) where there is a digital component:

1. Digital-to-Digital -- e.g. from a digital satellite transmission to a digital recording device;
2. Digital-to-Analog -- e.g. from a digital video disc to a VCR;
3. Analog-to-Digital -- e.g. from a videocassette to a digital recording device.

Unrestricted copying would be allowed from free TV and basic cable; one copy allowed from Pay TV (HBO); no copies allowed from prerecorded media (DVDs), Video-on-Demand and Pay per View.

MPAA/CEMA Agreement

In March of this year MPAA reached an agreement with the consumer electronics industry to support legislation that would mandate copy control circuitry in all digital recording devices, including general purpose computers. This proposal was resolutely opposed by the computer industry, which proposed as an alternative, a voluntary, encryption based copy control scheme, backed up by general anti-circumvention legislation.

Computer Industry Proposal

The computer industry proposal has some advantages over the MPAA/CEMA approach, principally because encryption will provide some additional measure of security against unauthorized copying. It also calls for much more simple, and therefore easier to enact, legislation.

However, there are significant technological hurdles that must be cleared to implement a voluntary encryption based system. Biweekly meetings are taking place among technical experts (numbering upwards of one

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hundred, primarily from the computer and consumer electronics industries). Matsushita has proposed an encryption system that is under serious consideration for incorporation in DVD players due to be on the market later this year and next. There is still no consensus on how to deal with transmissions, but several possibilities are being explored. A way to prevent analog-to-digital copying has not been found, although interim solutions are being considered.

Without going into the technical details, suffice it to say that the unresolved issues are many and complex. The basic question before us is whether we stay the present course; implement solutions as they become available, even if they are imperfect and incomplete; or do we abandon the effort, leaving the future to the actions of others.

Present Outlook

There appears to be a real commitment on the part of the consumer electronics industry, and on the part of most of the largest computer companies, to implement a voluntary, encryption based, copy control system to the extent such a system is technically feasible. At this moment, we have all of the major interests engaged in the effort to control copying, but it is a fragile process that could quickly fall apart as internal pressures among the various players make it more and more difficult to reach consensus.

Our window of opportunity is narrowing. Digital technology will reach the marketplace, and our movies will be distributed in this new format. In fact, movies are today distributed in digital format by direct broadcast satellite services. The present situation is not unlike the eve of pay TV or the VCR. Although some companies said they would never distribute through these new media, because they were loosely protected against piracy, inevitably the software followed the hardware into the marketplace.

A successful conclusion of the current discussions with the consumer electronics and computer industries will require MPAA member companies to exert a united commitment to reach agreement on the best solutions available.

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